

TIP REPORTING ALTERNATIVE COMMITMENT

between

Department of the Treasury-Internal Revenue Service

and

_____ [Name of Employer]

(Taxpayer-Employer's name, address, and identifying number) ("Employer") and the _____ District Director of Internal Revenue ("District Director") hereby agree to the following Tip Reporting Alternative Commitment ("TRAC").

The parties agree that the current law requirements for reporting cash and charge tips and for determining the Employer's liability for Federal Insurance Contribution Act ("FICA") taxes with respect to those tips operate as described below:

A. Section 6053(a) of the Internal Revenue Code of 1986, as amended ("Code"), requires employees to furnish one or more written statements to their employers reporting all tips received in each calendar month. The statements must be furnished to the employer by the 10th day of the following month. For purposes of both the employer and employee shares of FICA taxes, the tips are deemed to be "remuneration" at the time the employee's report is furnished to the employer. Section 3121(q) of the Code was amended by section 9006 of the Omnibus Reconciliation Act of 1987, Pub. L. No. 100-203, effective January 1, 1988, to cross-reference sections 3111(a) and (b) of the Code, thereby obligating employers to pay the employer share of FICA taxes on employees' tip income "remuneration". Accordingly, effective for tips received after 1987, an employer must pay its share of FICA taxes on the tip income reported to it by its employees under section 6053(a) of the Code at the time the income is deemed to be remuneration by section 3121(q) of the Code.

B. If an employee fails to report tip income to the employer as required by section 6053(a) of the Code, or underreports tip income to the employer, the employer's liability for the portion of FICA taxes attributable to such tip income is collectible only under the "notice and demand" procedure found in the last clause of section 3121(q) of the Code. Under this procedure, the Internal Revenue Service ("Service") provides a "notice and demand" to the employer to reflect tip income not previously reported by the employee to the employer. This tip income then becomes "remuneration" under section 3121(q) for purposes of determining the employer's share of FICA taxes under sections 3111(a) and (b) of the Code.

C. Section 6053(c)(3) of the Code requires every large food or beverage establishment to allocate among its tipped employees annually an amount equal to the excess of 8 percent (or a lower percentage if approved by the Secretary of the Treasury) of the establishment's gross receipts (other than nonallocable receipts) for that payroll period, over the aggregate amount of tips such employees reported to the establishment for that period. This allocated amount is reported on the employees' Forms W-2 for informational purposes only. A "large food or beverage establishment" for this purpose is any trade or business which provides food or beverages, with respect to which tipping the employees who serve the food or beverages is customary, and which normally employed more than 10 employees on a typical business day during the preceding calendar year. "Nonallocable receipts" are receipts allocable to carry out sales or to services with respect to which a service charge of 10 percent or more is added.

D. Under section 6652(b) of the Code, if an employee fails to report the tip income received in any calendar month as required by section 6053(a), the employee can be assessed a penalty equal to 50 percent of the additional employee FICA tax due with respect to the tip income, unless the employee can show that the failure is due to reasonable cause and not willful neglect.

In October 1993, the Service implemented nationally its Tip Rate Determination Education Program ("Program"). The purpose of the Program is to ensure maximum compliance by employees of food and beverage establishments with the provisions of the Code relating to tip income. To implement the Program, the Service designed a Tip Rate Determination Agreement ("TRDA"), which is an agreement between the Service and participating employers and their employees.

Representatives of the food service industry and the Service, in cooperation, developed a new agreement, the Tip Reporting Alternative Commitment Agreement ("TRAC agreement" or "Agreement"), to be entered into by the Service and participating employers. The TRAC agreement is an alternative to any existing TRDA or any TRDA that may be offered by the Service to an employer.

The Service will accept a TRAC agreement as an alternative to a TRDA in every District, will permit all eligible employers to enter into a TRAC agreement, and will assist applicants in understanding and meeting the requirements for participation in a TRAC agreement.

The District Director and the Employer have agreed to resolve disputes concerning the responsibilities of the Employer and the District Director under section 3121(q) of the Code and to establish procedures to prevent such disputes in the future. Therefore, the parties agree as follows:

I. DEFINITIONS

A. Employer means _____ [insert name].

B. Establishment means each of the food and beverage establishments listed by name, address, and identifying number in Attachment A. If the Employer has one place of business, that place of business is an Establishment.

C. Employee means a person employed by the Establishment who directly and or indirectly receives tips of at least \$20.00 per month during the course of the employee's employment (e.g., wait persons, bus persons, bartenders, and cocktail servers).

D. TRAC application means a signed request to enter into a TRAC agreement submitted by mail.

E. District Director means the District Director of Internal Revenue for _____ [insert District] or designee.

II. EFFECTIVE DATE OF AGREEMENT

A. General rule. Except as described below, this Agreement is effective on the first day of the first calendar quarter following the date the District Director signs the Agreement.

B. Special rules.

1. Employer with Establishment open to the public before June 1, 1995 -- Applications submitted before June 1, 1996. In the case of an Employer who (1) had one or more Establishments open to the public before June 1, 1995, and (2) submits its TRAC application before June 1, 1996, the TRAC agreement is effective on the first day of the first calendar quarter following the quarter in which the application is submitted to the District Director, unless the District Director rejects the application (with respect to any or all of the Establishments) in writing within 3 months after the date of submission. (Section II. B. 5. sets forth the reasons for which the District Director may reject a TRAC application.)

2. Employer with no Establishment open to the public before June 1, 1995 -- Applications submitted within 12 months after first Establishment opens. In the case of an Employer who (1) had no Establishment open to the public before June 1, 1995, and (2) submits its TRAC application within 12 months after its first Establishment opens to the public, the TRAC agreement is effective on the first day of the first calendar quarter following the quarter in which the application is submitted to the District Director, unless the District Director rejects the application (with respect to any or all of the Establishments) in writing within 3 months after the date of submission. (Section

II. B. 5. sets forth the reasons for which a District Director may reject a TRAC application.)

3. Employer acquisition or public opening of Establishment -- Participation and nonparticipation in Agreement. If an Employer currently participating in a TRAC agreement acquires or opens to the public an additional Establishment, the Employer must provide an addendum to Attachment A to the District Director within six months after the date of any such acquisition or public opening. The addendum will include the name, address, and identifying number of the acquired or opened Establishment. Such Establishment will be treated as participating in the TRAC agreement beginning on the date of acquisition or public opening, unless the District Director rejects the application in writing within three months after the date of submission of the addendum. If the Employer does not furnish a timely addendum, the general rule of Section II.A. applies.

4. Change in Ownership or Control. If an Employer or Establishment currently participating in a TRAC agreement undergoes a change in ownership or control, such Employer or Establishment must provide an addendum to Attachment A to the District Director within six months after the effective date of the change. The addendum will include the name, address, and identifying number of the acquiring entity. The acquiring entity will be treated as the successor Employer under the original TRAC agreement beginning on the date of change in ownership or control unless the District Director rejects the addendum in writing within three months of its submission, in whole or in part, for the reasons set forth in Section II. B. 5.

5. Rejection by the District Director. The District Director may reject a TRAC application or addendum for one of the following reasons:

a. the failure of the Employer to comply with the rules relating to the filing of any federal tax return, paying the amount of any undisputed federal tax, or making any deposit of federal taxes; or

b. the inability of an Establishment to comply with the procedures set forth in Section III.; or

c. the pursuit, by the Internal Revenue Service or another federal agency, of administrative or judicial action relating to the applicant or related party.

C. Ongoing tip examination or TRDA validation. A tip examination or TRDA validation in progress on the date the Employer submits its TRAC application will not affect the effective date of this Agreement.

III. COMMITMENT OF EMPLOYER

While this Agreement is in effect, the Employer agrees to the following provisions:

A. Educational Program. The Employer must institute and maintain for each calendar quarter an educational program which trains newly hired Employees and periodically updates existing Employees as to their reporting obligations with respect to tip income received as either cash tips or charged tips. This educational program may include on site or off site training by the Establishment, video programs, and written materials, such as tip reporting booklets offered as part of new employee informational materials.

This educational program must emphasize that, in addition to charged tips attributable to Employees, all cash tips paid to and retained by the Employees must be reported to their employing Establishment. The Employer may illustrate this by informing the Employees of the Establishment's charged sales to cash sales ratio and explaining that there is a correlation between charged tips and cash tips.

The Employer as part of this program must explain to the employees their obligation to maintain for their records the information required in the Form 4070A. This educational program also should advise all participants of the benefits of proper tip reporting (e.g., Social Security wage credit history, increased retirement plan contributions, and creation of adequate records of tip income).

B. Requirements regarding returns, taxes, and records.

1. Filing returns.

a. Form 941. Each calendar quarter, the Employer must comply with the requirements for filing Form 941, Employer's Quarterly Federal Tax Return. The Form 941 must include all charged and cash tips reported by the Employees to the employing Establishment(s) in accordance with the procedures set forth in Section III. B. 5.

b. Form 8027. For each Establishment that is a "large food or beverage establishment," the Employer must comply with the requirements for filing Form 8027, Employer's Annual Information Return of Tip Income and Allocated Tips, and send an additional copy of each Form 8027 to the District Director. If the total reported tips of the Establishment are less than 8 percent (or a lower percentage if approved by the Secretary of the Treasury) of the Establishment's gross receipts from food or beverage operations subject to tipping during the calendar year, the Employer will allocate tips for the Establishment under the procedures outlined in section 6053(c)(3) of the Code. Reported tips include tips attributed to and verified or corrected by Employees in accordance with the procedures set forth in Section III. B. 5.

c. Forms W-2. The Employer (or employing Establishment) must comply with the requirements for filing Forms W-2 for all the Employees and include all reported charged and cash tips on the Employees' Forms W-2, including tips verified or corrected pursuant to Section III. B. 5.

d. Other returns. The Employer must comply with the requirements for filing all other required federal tax returns.

2. Payment and deposit of taxes. The Employer must comply with the requirements for paying the amount of any undisputed federal tax that is due and depositing federal taxes.

3. Maintenance of records. Each Establishment, whether or not a "large food or beverage establishment," must maintain records of the following:

- a. Gross receipts subject to food or beverage tipping, and
- b. Charge receipts showing charged tips.

The Employer must retain these records for at least 4 years after the April 15 following the calendar year to which the records relate.

4. Availability of records. Upon the request of the District Director, the Employer will make the following quarterly totals available, by Establishment, for statistical samplings of its Establishments:

- a. Gross receipts subject to food or beverage tipping,
- b. Charge receipts showing charged tips,
- c. Total charged tips, and
- d. Total tips reported.

5. Employee tip-reporting procedures.

a. Charged Tips. Each Establishment must establish a procedure under which a written statement is prepared and processed on a regular basis (no less frequently than monthly), reflecting all charged tips for sales attributable to each directly tipped Employee. The Establishment must implement reasonable procedures under which each directly tipped Employee is given the opportunity to verify or correct any statement of proposed attribution of charged tips, in order to reflect tip outs, tip sharing, tip pooling, and other adjustments. For example, the Establishment would satisfy this paragraph if it provided a written statement that contained the following

information: Employee's charged sales, Employee's total charged tips, and the ratio, as a percentage, of charged tips to charged sales.

The Establishment must also adopt a reasonable method for reporting of charged tips received by indirectly tipped Employees. For example, the Employee may report to the Establishment the amount and with whom tips were shared. Alternatively, the directly tipped Employee may provide to the Establishment a copy of Form 4070A indicating the shared tips. As another example, the Establishment could furnish the indirectly tipped Employee a written statement, which that Employee would verify or correct in a manner similar to the procedure for directly tipped Employees.

The Employer's procedures must enable Employees to meet their reporting requirements under section 6053(a) of the Code. To meet these requirements, the Employee must sign the verified or corrected statement of attributed tips (no less frequently than monthly) and give the statement to the Establishment no later than the 10th day of the month following the month in which the Employee received the tips.

This verified or corrected statement (if completed by the 10th of the month for tips received during the preceding month) will satisfy the Employees' requirements of reporting charged tips to the Employer under section 6053(a). The Employer may satisfy the requirements of the section, if it remits charged tips to the Employees through the payroll system under a method that ensures reporting of tips by Employees and is consistent with sections 3102 and 3402 of the Code.

b. Cash Tips. Each Establishment must establish a procedure under which a written statement is prepared and processed on a regular basis (no less frequently than monthly), reflecting all cash tips for sales attributable to each directly tipped Employee. For example, if the Employee signs for charged tips on a daily basis, the Employee may record the amount of cash tips received at the same time. As another example, a procedure comparable to the procedure for charged tips would be appropriate for cash tips. The Employer may also provide a separate procedure for reporting cash tips.

IV. COMMITMENT OF DISTRICT DIRECTOR

A. General rule. Except as provided in B. below, any section 3121(q) notice and demand issued to the Employer (or Establishment) by the District Director shall be based solely on amounts reflected on one or more of the following forms:

1. Form 4137, Social Security and Medicare Tax on Unreported Tip Income, filed by an Employee with his or her Form 1040, or

2. Form 885-T, Adjustment of Social Security Tax on Tip Income Not Reported to Employer, prepared at the conclusion of an employee tip examination.

B. Special rules.

1. Retroactive revocation. In the event the District Director revokes the Agreement retroactively as provided under Section V. A. 1., the general rule of Section IV. A. does not apply.

2. Prospective revocation. In the event of a revocation under Section V. A. 2. or 3., or Section V. B., the general rule in Section IV. A. will apply with respect to tip income actually received by (or deemed under section 3121(q) of the Code to have been paid to) Employees at the Establishment during the period from the effective date of the TRAC agreement until the effective date of revocation.

3. Ongoing Tip Examination or TRDA Validation. If the District Director has initiated a tip examination or TRDA validation of one or more Establishments prior to the filing of the TRAC application, the District Director will not be bound by the general rule of Section IV. A., with respect to any tip income actually received by Employees at the Establishment during any calendar quarters under tip examination or validation. TRAC will be available to the Employer for all other calendar quarters as provided in this Agreement.

C. Compliance review. The District Director may not evaluate the Employer (or Establishment) for compliance with the provisions of Section III. A. (pertaining to the Employer's educational program) or Section III. B. 4. (pertaining to Employee tip-reporting procedures) until the second calendar quarter following the quarter in which this Agreement becomes effective. During the first two calendar quarters of this Agreement the District may review the Employer's (or Establishment's) progress in complying with the provisions of those Sections.

D. Examinations and/or inspections of books and records. The inspection of books of account or records pursuant to a tip examination or compliance review will not preclude or impede (under section 7605(b) of the Code, section 530(a)(2) of the Revenue Act of 1978, or any administrative provisions adopted by the Service) a later examination of a return or inspection of books of account or records with respect to any tax period involved in the tip examination or compliance review. The Service need not comply with any applicable procedural restrictions (for example, providing notice under section 7605(b)) before beginning such examination or inspection.

V. **REVOCATION**

A. Revocation by District Director. The District Director will revoke this Agreement only for the following reasons:

1. Failure to comply with Section III. A. or Section III. B. 5. If the District Director determines that the Employer (or any Establishment) has failed to substantially comply with Section III. A. (pertaining to the education program) or Section III. B. 5. (pertaining to employee tip-reporting procedures), the District Director may retroactively revoke this Agreement. The revocation will be effective the first day of the first calendar quarter of the Employer's (or Establishment's) substantial noncompliance. The District Director must notify the Employer in writing of the revocation and the Establishment(s) to which the revocation applies. If the revocation applies to all the Establishments of the Employer, the Agreement will be terminated, as of the above-stated effective date.

2. Failure to meet requirements of Section III. B. 1., 2., 3, and 4. If the Employer (or any Establishment) fails to meet any of the requirements of Section III. B. 1., 2., 3., or 4. (pertaining to filing returns, paying and depositing taxes, maintenance of records, and availability of records), the District Director may revoke this Agreement. The revocation will be effective the first day of the first calendar quarter after the District Director notifies the Employer in writing that the Agreement no longer applies to the Employer (or Establishment).

3. Employee underreporting of tips. If the District Director determines that the Employees of an Establishment have collectively and substantially underreported tip income for at least two continuous calendar quarters despite the Employer's (or Establishment's) substantial compliance with the procedures in Section III. B. 5. (employee-tip-reporting procedures), the District Director may revoke this Agreement with respect to the Establishment. The revocation will be effective the first day of the first calendar quarter after the District Director notifies the Employer in writing that the Agreement no longer applies to the Establishment. If the revocation applies to all the Establishments of the Employer, the Agreement will be terminated, as of the above-stated effective date.

4. Other. In addition to the reasons for revocation listed in this section, the District Director may revoke the Agreement when the Internal Revenue Service or another federal agency pursues an administrative or judicial action relating to the Employer or Establishment that is a party or related party to this Agreement.

B. Revocation by Employer. If the Employer no longer wishes this Agreement to apply to one or more Establishments, the Employer may revoke this Agreement with respect to the Establishment(s), by providing written notification to the District Director identifying the Establishments(s). The revocation by the Employer will be effective the first day of the first calendar quarter after the Employer notifies the District

Director in writing. If the revocation applies to all the Establishments of the Employer, the Agreement will be terminated, as of the above-stated effective date.

C. Reapplication by Employer. If the District Director revokes this Agreement either with respect to the Employer or with respect to an Establishment(s), the Employer may submit a new TRAC application. In the event of a reapplication, the effective date provided in Section II. A. will apply.

VI. MISCELLANEOUS

A. Notices. All correspondence pertaining to this Agreement, including a notice of revocation, must be sent to the parties to this Agreement at the addresses stated below, unless notified in writing of a change of address. In the event of a change of address, all correspondence must be sent to the new address.

B. Authority. The Employer represents that it has the authority to enter into this Agreement on behalf of itself and the Establishment(s) listed in Attachment A.

C. Date of notices. All notices and TRAC applications are deemed to be sent or submitted on the date of the postmark stamped on the envelope or, in the case of a notice or application sent by certified mail, the sender's receipt.

D. Statutory changes. The Commissioner may terminate this Agreement at any time following a significant statutory change in the FICA taxation of tips.

E. Sunset provision. The Commissioner of Internal Revenue may terminate prospectively the Tip Rate Determination Education Program or TRAC agreements after May 31, 2000.

VII. PAPERWORK REDUCTION ACT

The collections of information contained in this document have been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-1549.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number. The collections of information in this document are in sections I.B., I.D., II.B.3. and 4., III.A., III.B.3. and 4., III.C., and V.B. This information is required to comply with sections 6053(a) and 6001 of the Internal Revenue Code and to assist the Internal Revenue Service in its compliance efforts. This information will be used to monitor the Employer's performance under the Agreement. The collections of information are required to obtain

the benefits available under the Agreement. The likely respondents are business or other for-profit institutions.

The estimated total annual reporting and/or recordkeeping burden is 237,881 hours.

The estimated annual burden per respondent/recordkeeper varies from 12 hours to 51 hours, depending on individual circumstances, with an estimated average of 40 hours. The estimated number of respondents and/or recordkeepers is 6,000.

The estimated annual frequency of responses (used for reporting requirements only) is on occasion.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by section 6103 of the Code.

VIII. SIGNATURES

By signing this Agreement, the parties certify that they have read and agreed to the terms of this document, including Attachment A, Names, Addresses, and Employer Identification Numbers by Employer of Establishments Covered Under TRAC Agreements.

EMPLOYER:

INTERNAL REVENUE SERVICE

(Name of Employer)

_____ District

(Signature)

(Signature)

BY: _____

BY: _____
(Director's Name)

TITLE: _____

TITLE: District Director

ADDRESS:

ADDRESS:

(Street address - Headquarters)

(Street address)

(City, state, ZIP code)

(City, state, ZIP code)

DATE: _____

DATE: _____